



# DEPARTMENT OF JUSTICE

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## BANK MERGERS--ANTITRUST TRENDS

Addressed by

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Before the

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Our nation's economic vitality depends upon the financial soundness and competitive structure of the banking industry. For it is the banking industry upon which American consumers and businesses rely for credit. And experience has shown that where there are competing sources of credit, the price of that credit is lower and its availability is better. That rivalry also brings consumers the benefits of greater innovation and better quality financial services.

Antitrust policy plays the role of ensuring that competition flourishes. And in my view, the bank merger program of the Department of Justice has successfully prevented anticompetitive effects from bank mergers, ensuring that competitive options are preserved, while at the same time permitting most of the efficiencies associated with those mergers. The Department of Justice's role, unlike that of our sister agencies which also address competitive issues, is as a law enforcement agency, not as a regulator. We intervene only when we believe it is necessary to ensure that markets remain competitive.

The Division has been extraordinarily active in this area, dealing with the unprecedented merger wave, which has included a large number of very large bank mergers.<sup>1</sup> During Fiscal Year 1995, the Division screened almost 1,900 bank mergers, and issued 1,211 competitive factor reports, and so far in 1996, we have screened 1,659 mergers and issued 1,096 competitive factor reports. In 1995, we required divestitures in five cases. So far in 1996, we have required divestitures in six cases.<sup>2</sup> These numbers likely understate the Division's influence in bank mergers because our clearly articulated bank screens deter many bank mergers that would

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<sup>1</sup> Both the numbers of mergers and the dollar value of mergers have increased dramatically. The number of mergers has risen from 5,651 in 1990 to 9,110 in 1995, a 61% increase. The value of mergers has increased from \$185.8 billion in 1990 to \$501.8 billion in 1995, a 170% increase. In 1995 we had more filings that could have been subject to a request for information than in any year since Hart-Scott-Rodino Act was implemented. And 1996 looks like it will surpass that record.

<sup>2</sup> Fleet Financial Group/Shawmut National Corporation; U.S. Bancorp/West One; First Bank System/First Interstate Bancorp; Wells Fargo/First Interstate; Corestates Financial/Meridian Bancorp; and Bank of Boston/Bay Banks.

contravene the antitrust laws. And we will continue to be vigilant watchdogs in the bank merger area.

Today I'd like to talk about how the Antitrust Division analyzes bank mergers generally. I'd also like to spend some time discussing how we've been able to resolve successfully a number of competitive concerns with targeted divestitures.

We've made great strides in clarifying our policies and are proud of that effort. The Bank Merger Screening Guidelines, issued jointly last year by the Division, The Federal Reserve Board and the Office of the Comptroller of the Currency, clarify the agencies' processes and, in a single document, set out the ground rules for the agencies' review of mergers.

In practice, these Screening Guidelines have ensured that bank merger applications come to us with the information necessary for us to review them and reach an initial assessment of a merger's likely competitive effects. The Division has also been willing to meet with parties before they file an application in order to discuss the likely impact of our screening process on a specific transaction. The Guidelines and our openness to advance consultation with the parties have enabled us to identify potential areas of concern and have allowed us and the other agencies to begin an examination and analysis of the competition issues and possible resolutions at an early stage.

In addition, we have sought to make it clear that these screens are not hard and fast rules or bright lines. Rather, they are meant to open the discussion and dialogue. The screening materials should inform the industry of the factors we will be examining and the issues that are important to our evaluation. But it does not follow that we will challenge a proposed merger merely because it fails the tests in the screens. Indeed, less than one percent of all applications raise any significant antitrust concern under the screening procedures. The primary effect of our Screening Guidelines is to allow transactions that raise no significant antitrust issues to proceed promptly.

Cooperation among the agencies has also produced a wide range of other benefits. For example, the lines of communication and dialogue among the agencies has improved substantially. To the extent the agencies are aware of each others' concerns, the parties can be more comfortable that the investigations are proceeding on parallel tracks, minimizing the potential for divergent decisions. Each agency also provides its own experience and perspective and often may pursue issues related, but not identical, to those of other agencies. The communities in which bank mergers occur should be reassured that a variety and range of concerns are being investigated and addressed.

In that connection, the participation of State Attorneys General in joint investigations with the Division has proven to be extremely helpful and productive. The State Attorneys General are able to bring to the investigations knowledge of local market conditions and concerns, as well as knowledge of local businesses and their needs. I believe this knowledge has allowed our investigations to proceed more effectively and has resulted in decisions and resolutions which better address local issues.

The Antitrust Division reviews bank mergers within the same analytic framework (our Merger Guidelines of April 2, 1992) that we use for mergers in other industries--whether those are airlines, telecommunications, or banks. Within this framework we have relied on our experience with numerous banking transactions to develop certain factual conclusions that guide our analysis. In the banking industry, we have focused upon the availability of banking services, including loans and credit, to small and medium-sized businesses.

Our investigations have suggested that other than commercial banks, small and medium-sized businesses have few alternatives available to them for their credit needs. Small businesses tend to have credit needs that do not attract banks located in other regions and tend to rely on and value their relationships with their local commercial bankers. Medium-sized businesses may be able to access lenders and providers from larger areas, but still tend not to have the access to national capital markets that may be available to larger corporations. I note that we are

continuously evaluating market evidence to see if this continues to be the case. We will continue to monitor attempts to "score" small business loans (to assess credit risk) and to securitize small business credits to see if these efforts enlarge the substitutes available to businesses. Small businesses rely on non-banks, out-of-market banks, or non-commercial banks for financing to a significant extent in the case of mortgages, or vehicle and equipment loans, but much less so for lines of credit. The Federal Reserve's '93 Survey of Small Business Use found that 74% of the businesses surveyed had credit lines, loans, or capital leases obtained from depository financial institutions. Looking only at lines of credit, 88% of businesses that had lines of credit obtained them from depository financial institutions (lines of credit were obtained from commercial banks by 81% of businesses that had lines of credit).

Given that small businesses tend to bank locally, we have focused our analysis for small business banking services primarily within defined local areas such as RMAs (Ranally Metropolitan Areas) or counties as an approximation of the geographic scope of competition. Once we have identified a relevant geographic market, we will use the deposits of commercial banks in the area as the best initial proxy to measure the competitive significance of the merging banks. A thrift's deposits are excluded in our first review, but then added if our investigation discloses that the thrift is, in fact, making commercial loans. Although we use the same methodology for our analysis of lending to medium-sized businesses, the effective area of competition by banks for such loans and services tends to be larger than for small businesses because of the greater ability of banks to secure and service those loans over greater distances.<sup>3</sup>

In each investigation we conduct, we look for the choices consumers really have if, after a merger, prices go up a small but significant amount. If you're getting a small business loan, say for working capital, from a commercial bank, and if prices go up 5-10%, what choices do

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<sup>3</sup> For example, in the Bank of America/Security Pacific merger, "middle market" consisted of businesses with sales of \$10 million to \$100 million and credit needs of between \$1 million to 10 million. In the Comerica/Manufacturer (unchallenged) merger in Detroit, "middle market" customers had sales of \$5 million to 50 million.

you have? A finance company? Probably not, those loans today are more than 10% higher than those of a commercial bank. A credit union? No. credit unions haven't to date made working capital loans. An S&L? Maybe. And our investigation will see what they are really doing and what they likely will do in the next 2 years.

I would like to stress that our focus on business banking services does not mean that we are ignoring the potential effects of bank mergers on retail consumers. We have found that retail consumers have banking alternatives available to them that most business customers do not--such as thrifts and credit unions. Although these factors may diminish potential anticompetitive effects, we have and will continue to screen and investigate for any significant loss of competition in the retail area as well.

Whenever we conduct detailed investigations, we seek to learn as much as we can about competition for banking services in the relevant markets. We specifically take into account, for example, the actual level of commercial loan activity by the market participants. I should add a note of caution on this point--that the loan data may not substitute for the deposit data. The deposit data historically have been more reliable and loan data have not necessarily reflected lending capability or the full competitive significance of a commercial bank in the market.

We treat all of the issues raised about the future of the industry seriously. But the focus of the Merger Guidelines is not what may happen in a market in five or ten years, but what is happening today and over a short two-year time horizon. Since our review is fact driven, I think it is fair to say that when we see major changes in the market, those changes will be reflected in our analysis. This is because antitrust merger analysis is flexible and easily adapts to a dynamic market. Over time, we will continue to evaluate market changes and our internal review process, as appropriate, will reflect industry conditions.

As you know, there are studies showing that concentration has an effect in the banking industry. As a result, we will likely take a hard look at certain increasingly concentrating regions and markets, especially where a merger would leave a metropolitan area with one or two dominant firms and a fringe of small independent banks which may not be able to compete

significantly for small and medium-sized business loans. In these markets, as in our typical investigations, there are not bright line tests. Instead, I anticipate that we will consider a number of factors, none alone being determinative, in evaluating potential competitive effects. These factors include: deposit concentration figures, branch networks, entry and the ability of small firms to expand quickly.

Further, we are increasingly evaluating the potential effects of bank mergers on middle market banking customers. Such customers have banking needs that are different from small businesses, such as significantly higher capital needs and access to more sophisticated cash management services. Similarly, banks that can offer services to small businesses may not be able to offer the necessary services to middle market businesses, in part because of regulatory and in-house lending limits. The critical issue that we examine, and which based on a factual investigation may result in different conclusions in different matters, is the geographic scope of competition, including the ability of firms to compete effectively through LPOs (loan production offices).

After we determine the relevant markets and assess likely competitive effects, we also look at the possibility of entry and expansion. In many cases this factor can be determinative. Here we are again looking at market facts: What has been the history of entry? Has there been de novo entry. If there has been entry, how successful is it? Who has plans to enter? Is the area grouping rapidly. As far as efficiencies go, we always consider them carefully, and know that they can be a major benefit of some mergers. In a number of the anticompetitive bank mergers we have reviewed, most of the savings claimed were not unique to the merger, and could have been achieved in other ways.

Though I'm sure this is something you know, I'd like to emphasize today that in the few cases each year where we conclude that divestitures are required, we try to create solutions that both resolve our concerns and ensure that the merging parties obtain the efficiencies of the deal. At the beginning of fiscal year 1996, the Department secured a major divestiture in the proposed

acquisition of Shawmut National Corporation by Fleet Financial Group. Our analysis of this proposed merger of two of the largest New England banking systems revealed that it would raise antitrust concerns in 14 geographic markets in four states. After extensive negotiations, the parties agreed to divest to various buyers 64 offices holding about \$3 billion in deposits. The divestiture was the second largest ever in the bank merger context, and the largest in a single market (Hartford, Connecticut, \$1.6 billion in deposits). Our investigation of this merger was closely coordinated with the states of Connecticut and Massachusetts, who provided us important information about local market conditions and effective relief alternatives. Fleet's acquisition of Shawmut, Wells Fargo's acquisition of First Interstate, U.S. Bancorp's acquisition of Bank One and CoreState's acquisition of Meridian and Bank of Boston's acquisition of BayBanks<sup>4</sup> also all proceeded to closing after we negotiated appropriate divestitures that solved competitive concerns with discrete local markets. Each of those matters was coordinated with the states who provided us with valuable information about local market conditions and effective relief alternatives.<sup>5</sup> Moreover, in the First Interstate transaction, we took care during the phase when the transaction was subject to competing tender offers not to favor one party over the other. We will continue an even-handed approach so that our review procedures do not provide any unnecessary advantage to either side.

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<sup>4</sup> Bank of Boston/Baybanks.

<sup>5</sup> --Wells Fargo & Company's acquisition of First Interstate Bancorp was conditional on the divestitures in 30 markets of 61 offices with deposits of \$2.5 billion.

--U.S. Bancorp's proposed merger with West One Bancorp raised competitive concerns in ten geographic markets in Oregon and Washington; the merging parties agreed to divest 27 offices (six in Washington and 21 in Oregon), holding \$514 million in deposits.

--CoreStates Financial Corp's acquisition of Meridian Bancorp Inc. raised antitrust concerns in two Eastern Pennsylvania markets; the parties agreed to divest 11 branch offices with deposits of about \$444 million.

--Bank of Boston's acquisition of BayBanks Inc. raised antitrust concerns in the Boston market; the parties agreed to divest 20 offices within \$860 million in deposits.



Last week I was sent a newspaper article commenting on a divestiture in the Bank of Boston/BayBanks deal. The article said that UST, the purchaser of the divested branches has now become a true metropolitan banking franchise--specializing in small commercial lending and consumer banking. That's the type of success story we're delighted to report, and it illustrates and underscores the success of antitrust enforcement in the 90s.

One final point concerning divestitures is that when we construct a network of branch offices to find an appropriate fix to potential competitive concerns, we will look beyond the amount of assets to be divested to the quality and location of the branches that are included in the divestiture package. Because our primary focus has been competition for small business loans, we investigate in some detail the characteristics of the parties' branches in those markets, including their deposit and loan make-up, locations and ease of access for businesses. Our goal is to determine and evaluate each branch's overall current use by, and potential attractiveness to, area businesses. We have requested some parties, for example, to provide photographs of the branches. We also obtain significant additional information during our interviews of other participants in the market.

We also spend considerable time evaluating the viability and overall effectiveness of branch networks proposed for divestitures in a market. The issue we address is whether a purchaser of the network would be an effective business banking competitor in the area. The factors we consider include the number and location of branches as well as the needed mix of deposits, banking services and personnel. The result is not based solely on concentration figures. We may argue strongly for particular branches or branch locations to be included in the divestiture package. We also require that parties divest the entire relationship for each customer associated with each branch, including deposits, loans and other related services. The final package is intended to reflect the commercial realities of the markets involved, as well as to give the purchaser of the divested branches a strong presence in the market.

Everybody benefits from our policy of working with the other federal agencies, state officials and the merging banks: the governmental agencies get the information they need more quickly, the merging banks are more likely to receive uniform treatment from the various governmental agencies involved without the expense and uncertainty of litigation, and consumers of banking services are more adequately protected from competitive harm. In sum, bank merger policy in the '90s is a win-win situation for all.